Cepi RENEWABLE RECYCLED RESPONSIBLE EUROPEAN PAPER

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CEPI response to the public consultation on the draft

“Guidelines on certain State aid measures in the context of the system for greenhouse gas emission allowance trading post 2021”

Cepi is the European association representing the pulp (NACE code 17.11) and paper (NACE code 17.12) industry. Our industry welcomes the possibility to comment on the draft Guidelines on certain State aid measures in the context of the system for greenhouse gas emission allowance trading post 2021.

Comments from our sector are grouped around three areas: (1) eligibility, (2) proportionality, and (3) conditionality.

1) Eligibility

Cepi welcomes that both pulp (NACE 17.11) and paper (NACE 17.12) have been recognised among the sectors most at risk of carbon leakage. Both our sectors are electro-intensive and compete at international level. It is therefore important to safeguard their competitiveness, while we pursue our efforts in both decarbonising our operations and provide an ever-growing amount of products and solutions to decarbonise other segments of the European economy.

It will be therefore of utmost importance that compensation is granted to our sectors in all Member States. In this respect, **we strongly oppose to the introduction of the new paragraph 21 of the draft state aid**. Paragraph 21 allows Member States to exclude eligible sectors from being compensated “on the basis of objective, non-discriminatory and transparent criteria”.

There is a fundamental difference between the choice of a country to grant aid – or not – to eligible sectors, and the choice to grant aid only to certain sectors within the list of eligible sectors.

The possibility to exclude sectors is a novelty which was not present in the current state aid guidelines for the post-2012 ETS trading period (SWD(2012) 130 final) (SWD(2012) 131 final), nor in the more recent state aid guidelines on energy and environment for the period 2014-2020 (OJ C 200, 28.6.2014, p. 1-55).

If maintained, the provision would deliver the follow negative consequences:

1. It creates regulatory instability. While the proposed new guidelines are intended to provide regulatory stability, the specific provision acts in the opposite direction. It places individual sectors under the threat of being excluded at any time during the trading period, suddenly exposing them to unforeseen carbon costs.

2. It is against the principles of the ETS, whereby a sector deemed to be exposed to the risk of carbon leakage is eligible to receive carbon leakage protection in every single country in the EEA. There should be no possibility for a single member state to derogate from such provisions.

3. Increases the risk of negatively affecting the international competitiveness of European industries. Every sector recognised at risk of carbon leakage should be protected in every country in Europe.

2) Proportionality

As a matter of principle, compensation for indirect carbon costs, as well as for direct carbon costs, needs to ensure an effective protection against the risk of carbon leakage.

In this respect, it is still not possible to assess to what extent the draft guidelines would deliver the necessary level of protection. Many values in the formula are still missing: percentage reduction in the 'fall back electricity consumption efficiency benchmark', limit to the amount of indirect carbon costs paid by undertakers in certain sectors, minimum regional CO_2 emission factors. These values will be crucial to calculate the final amount of aid granted to undertakings.

As a matter of principle, compensation for carbon costs in electricity prices should reflect the exposure to carbon cost passed into electricity prices. No distinction should be made between costs incurred and opportunity costs.

In this respect, **we support the Commission decision to keep the definition of 'CO_2 emission factor'** as *"the weighted average of the CO_2 intensity of electricity produced from fossil fuels in different geographic areas"*, as it is the case already in the current state aid guidelines valid until 2020.

At the same time, we have **concerns over the proposed new boundaries of the regional zones** (Annex III), compared to the ones identified in the current state aid guidelines. The rationale, as explained in the report produced by the consultant, is that despite further market integration and market coupling, the price convergence has decreased. And, always according to the consultant, price convergence is "*the only factor that reflects whether two neighbouring markets shared similar indirect carbon costs.*"

We disagree with the consultant's conclusions. The first element to be looked at is the correlation in price movements between interconnected markets. The price convergence, as acknowledged also by the consultant, can be the result of several factors. But that doesn't necessarily prove the lack of correlation between two zones in the price formation.

As a matter of principle, the allocation of emission factors should contribute to promoting a' level playing field' among Member States and in line with the Single Electricity Market.

In identifying the relevant zones, we would invite the Commission to run an ex ante and ex post evaluation of the methodology applied to historic data. And, in case of divergence, reassess the zone boundaries accordingly.

Cepi also noted the new provision that gives the **possibility to Member States to limit the amount of the indirect costs to be paid by undertakers**, should the aid intensity of 75% be inadequate. This provision mirrors the approach that has already been introduced in the state aid guidelines on energy and environmental protection (EEAG). Moreover, from what stated in the consultant's report, such provision could be beneficial in limiting the indirect costs for our industry.

While we welcome such possibility, we think the provision needs further clarifications, also in view that the two guidelines are different in nature: while the ETS guidelines retroactively compensate for a cost already incurred, the EEAG caps upfront the additional costs. Specifically:

1. It should be clear that "undertaking" refers to "company" and not to "installations". If otherwise, the provision would raise major market distortions.[1]

[1] For instance, two installations producing the same product using the same amount of electricity, would receive a different level of compensation just to the different nature of their legal entity. Examples in this direction include cases when GVA is calculated at the installation or at headquarters level, or whether other activities not related to the production process take place at the industrial site (conversion of products, R&D centres…) leading to higher GVA values.

2. It should be clarified that the possibility for Member States to cap indirect costs is an additional measure that comes on top of the provision to grant aid intensity of 75%, should the latter not suffice to protect against the risk of carbon leakage. In other words: no installation is compensated less than 75% of CO_2 cost.

3) Conditionality

Our sector is strongly committed to improve energy efficiency and reduce both our direct and indirect emissions. We are already periodically reporting on our investments in promoting energy efficiency and renewable energy sources in our installations.[2]

The partial compensation and high electricity prices, coupled with internal and international market competition, are already sufficient drivers to push companies in implementing energy efficiency measures. Moreover, compensation for carbon costs passed into electricity prices is already partial and set at the level of benchmark setter. Meaning that even the best performer is subject to carbon costs due to partial compensation. The system has therefore already an embedded mechanism requiring undertakers to minimise the impact of carbon costs.

This is the reason why we find the provisions on conditionality (paragraph 54) unhelpful and potentially also counter-productive.

Specifically, concerning provision (a) in paragraph 54, there will be cases where the investment, even if proportionate, cannot be implemented. That could be the case, for instance, if no budget is available, or if market conditions require other strategies to remain competitive. Moreover, forcing investing in incremental efficiency measures could prevent investments in radical transformative measures, leading to stranded assets and/or drying up resources for projects with longer payback times.

Concerning provision (b) in paragraph 54, companies are already contributing in reducing the carbon footprint of their electricity consumption. Installing on-site renewable energy generation is a way to reduce direct carbon emissions. The number of companies signing Power Purchasing Agreements (PPAs) is growing. But this is done on a market-based approach. Forcing companies to sign PPAs creates a market unbalance, weakening the position of companies seeking for compensation from carbon costs in electricity prices and, conversely, strengthening the position of renewable energy suppliers. When a supplier is in a relatively stronger position than a consumer, competition is negatively affected.

Likewise, provision (c) in paragraph 54 is also extremely unhelpful. It assumes that a company is first exposed to the full amount of indirect costs and, when the amount to compensate those costs is available, it cannot be used to compensate those costs but rather used to invest in major projects. In other words, the company has the choice between “not being compensated for the carbon costs incurred”, or “not being compensated for the carbon costs incurred but receiving partial financing and being forced to used it to make additional investments”. In both cases – the company won’t be compensated for the carbon costs already incurred.

[2] http://reinvest2050.eu/